

Decision _____

BEFORE THE PUBLIC UTILITIES COMMISSION OF THE STATE OF CALIFORNIA

Application of Suburban Water Systems (U339W) for Authority to Issue, Sell and Deliver its First Mortgage Bonds Not Exceeding \$25,000,000 Principal Amount.

Application 14-12-011
(Filed December 15, 2014)

**DECISION AUTHORIZING SUBURBAN WATER SYSTEMS
TO ISSUE UP TO \$25 MILLION OF NEW FIRST MORTGAGE BONDS****Summary**

This decision grants Suburban Water Systems (Suburban) the authority to issue, sell and deliver up to \$25 million of new First Mortgage Bonds (Series F).¹ Suburban is also granted authority to: 1) execute a Sixth Amendment and Supplement to its existing Indenture of Mortgage and Deed of Trust and issue a Bond Purchase Agreement associated with the issuance of new First Mortgage Bonds; 2) be exempt from the Commission's New Financing Rule; and 3) use the First Mortgage Bonds authorized herein for proper purposes, including payment to its parent company, SouthWest Water Company, for monies expended on Suburban's behalf, and to pay for future expenditures related to construction, completion and improvement of utility plant.

By authorizing Suburban to issue \$25 million in bonds, Suburban can continue to fund its water distribution system pursuant to Public Utilities Code Section 451, which requires Suburban to take all actions "... necessary to promote

¹ First Mortgage Bonds are a form of long-term debt.

the safety, health, comfort and convenience of its patrons, employees and the public.”

1. Background

Suburban Water Systems (Suburban) is a Class-A water utility subject to the jurisdiction of this Commission, providing water service in portions of Orange and Los Angeles counties, comprising all or part of all of Glendora, Covina, West Covina, Walnut, La Puente, Hacienda Heights, City of Industry, Whittier, La Mirada, La Habra, Buena Park, and other unincorporated areas. Suburban owns wells, pumping equipment, water treatment equipment, reservoirs and tanks, transmission mains, distribution mains, meters, hydrants, land, water rights, and other property necessary for the conduct of business. Suburban is a wholly owned subsidiary of SouthWest Water Company (SouthWest).

On December 15, 2014, Suburban filed Application (A.) 14-12-011 requesting authorization to issue, sell, and deliver \$25 million of First Mortgage Bonds. On December 18, 2014, Resolution ALJ 176-3348 was issued, preliminarily categorizing this application as ratesetting and preliminarily determining that no hearings were needed.

No protests or responses to the application were filed.

On February 2, 2015, Suburban responded to the assigned Administrative Law Judge’s (ALJ) January 22, 2015 electronic mail ruling requesting information.

2. Request

Suburban seeks authorization to issue, sell, and deliver up to \$25 million of First Mortgage Bonds to meet its future financing needs based on a long-term forecast covering the five-year period 2015 through 2019. Suburban plans to use the proceeds to pay its parent company, SouthWest, for monies expended on

Suburban's behalf, and to pay for future expenditures related to construction, completion and improvement of utility plant. Suburban also seeks authority to: 1) encumber its utility assets pursuant to Public Utilities (Pub. Util.) Code § 851, in order to secure its new First Mortgage Bonds; and 2) receive an exemption from the New Financing Rule adopted in Decision (D.) 12-06-015, based on its request in the current application being less than \$42 million.

Specifically, Suburban plans to: 1) refinance a \$12,376,000 short-term treasury draw from its parent, SouthWest, which was expended for the design, construction, completion, extension or improvement of utility plant facilities and to repay short-term indebtedness incurred for such purposes; and 2) use the remaining proceeds to finance a portion of Suburban's annual capital expenditure program from 2015 through 2019. Suburban states that these expenditures are necessary to allow it to continue to provide safe and reliable water service to its customers.

Suburban plans to place the First Mortgage Bonds privately with one or more institutional investors. Because of changing market conditions, Suburban requests Commission authority to offer First Mortgage Bonds with negotiated terms and interest rates based on market conditions existing at the time of the placement. The new Series F First Mortgage Bonds issued by Suburban would:

1. Be direct obligations of Suburban;
2. Rank equally with other of Suburban's First Mortgage Bonds issued under the Indenture;
3. Have semi-annual interest payments;
4. Be redeemable prior to maturity, in whole or in part:
 - (a) at the option of Suburban at any time on not more than sixty and not less than thirty days prior notice, at par plus accrued interest, plus the Make-Whole Amount, if any, and

(b) upon receipt of proceeds equal to or exceeding \$25,000,000 by the trustee under the Indenture as a result of a casualty or condemnation, at the option of Suburban at par plus accrued interest, without the Make-Whole Amount;

- a. The Make-Whole Amount is the excess amount of the discounted value of the remaining scheduled payments for the principal called for redemption over the amount of such called principal.
- b. The Make-Whole Amount may in no event be less than zero. For purposes of the discounted value, the rate is equal to the interpolated yield of a U.S. Treasury security with a maturity equal to the remaining life of the called bonds + 50 basis points.

The Bond Purchase Agreement associated with the issuance of First Mortgage Bonds by Suburban would contain provisions similar to the Bond Purchase Agreement dated October 20, 2006 between Suburban and the Purchaser named therein for Suburban's (Series E) First Mortgage First Mortgage Bonds, with updated provisions for the specific conditions in place at the time it is issued. The Sixth Amendment and Supplement to Suburban's existing Indenture of Mortgage and Deed of Trust would contain similar provisions to the provisions contained in the Fifth Amendment and Supplement to Indenture dated October 20, 2006, pursuant to which the (Series E) First Mortgage Bonds of the Company were issued with updated provisions for the specific conditions in place at the time it is issued.

3. Discussion**3.1. Public Utilities Code Requirements for Issuance of Securities**

Suburban's request is subject to Public Utilities (Pub. Util.) Code §§ 816, 817, and 818.² The Commission has broad discretion under Pub. Util. Code §§ 816, et seq., to determine if a utility should be authorized to issue debt. Where necessary and appropriate, the Commission may attach conditions to the issuance of debt and stock to protect and promote the public interest.

Pursuant to Public Util. Code § 817, a public utility may only issue and use financing for selected purposes.³ Those purposes not listed in Pub. Util.

² Unless specified otherwise, all subsequent code section references are to the Public Utilities Code.

³ Section 817: A public utility may issue stocks and stock certificates or other evidence of interest or ownership, and bonds, notes, and other evidences of indebtedness payable at periods of more than 12 months after the date thereof, for any one or more of the following purposes and no others:

- (a) For the acquisition of property.
- (b) For the construction, completion, extension, or improvement of its facilities.
- (c) For the improvement or maintenance of its service.
- (d) For the discharge or lawful refunding of its obligations.
- (e) For the financing of the acquisition and installation of electrical and plumbing appliances and agricultural equipment which are sold by other than a public utility, for use within the service area of the public utility.
- (f) For the reorganization or readjustment of its indebtedness or capitalization upon a merger, consolidation, or other reorganization.
- (g) For the retirement of or in exchange for one or more outstanding stocks or stock certificates or other evidence of interest or ownership of

Footnote continued on next page

Code § 817 may only be paid with funds from normal utility operations. Suburban has substantiated that the issuance of First Mortgage Bonds is necessary for payment to its parent company, SouthWest, for monies expended on Suburban's behalf, and to pay for future expenditures related to construction, completion and improvement of utility plant. These purposes are authorized by Pub. Util. Code § 817 and, as required by § 818, are not reasonably chargeable to operating expenses or income.

Consistent with Pub. Util. Code § 824, Suburban shall maintain records to identify the specific long-term debt issued pursuant to this decision, and demonstrate that proceeds from such debt have been used only for public utility purposes.

Therefore, we will grant Suburban authority under Pub. Util. Code §§ 816 et seq. to issue new (Series F) First Mortgage Bonds for the aforementioned purposes, and for the amounts determined in this decision.

3.2. Forecast of Sources and Uses

Utility applications seeking authority to issue debt or other securities are based, in part, on forecasted sources and uses of funds that illustrate the

such public utility, or bonds, notes, or other evidence of indebtedness of such public utility, with or without the payment of cash.

(h) For the reimbursement of moneys actually expended from income or from any other money in the treasury of the public utility not secured by or obtained from the issue of stocks or stock certificates or other evidence of interest or ownership, or bonds, notes, or other evidences of indebtedness of the public utility, for any of the aforesaid purposes except maintenance of service and replacements, in cases where the applicant has kept its accounts and vouchers for such expenditures in such manner as to enable the commission to ascertain the amount of money so expended and the purposes for which such expenditure was made.

requested need for funding. Suburban used a long-term forecast covering the five-year period of 2015-2019 to determine its future financings needs.

Suburban's forecast includes uses of funds such as capital expenditures and to refinance a treasury draw from its parent. Suburban's forecast also includes sources of funds, such as cash flow from operations. Suburban states that it has no previously authorized financing authority remaining⁴ to offset its current request.

Table 1
Sources and Uses

USES OF FUNDS	(Thousands of Dollars)					
	2015	2016	2017	2018	2019	Total
Construction	\$13,364	\$15,064	\$15,064	\$13,272	\$13,291	\$70,055
Reimburse Treasury	\$12,376	0	0	0	0	\$12,376
Total Uses of Funds	\$25,740	\$15,064	\$15,064	\$13,272	\$13,291	\$82,431
SOURCES OF FUNDS						
Cash from Internal Sources and Short-Term Borrowing	\$9,812	\$11,918	\$12,557	\$11,766	\$11,379	\$57,432
Total Source of Funds	\$9,812	\$11,918	\$12,557	\$11,766	\$11,379	\$57,432
Surplus (Deficient) Financial Sources[1]	(\$15,928)	(\$3,146)	(\$2,507)	(\$1,506)	(\$1,912)	(\$24,999)

[1] Surplus (deficit) equals total financial requirements less total source of funds.

⁴ D.92-01-026, D.04-04-051, and D.06-10-022.

The Commission authorizes Suburban to issue \$25 million of new First Mortgage Bonds. This new financing will allow Suburban to fund its capital expenditure plans for the period 2015 through 2019, for capital expenditures and to refinance Suburban's treasury draw from its parent.

A granting of financing authority to a utility does not obligate the Commission to approve any capital projects. This financing authority provides Suburban with sufficient liquid resources to timely finance its upcoming public utility projects and to refinance Suburban's treasury draw from its parent. Review of the reasonableness of capital projects occurs as needed through the regulatory process applicable to each capital project. Therefore, approval of this financing request does not prejudice any of Suburban's forecasted projects for the period 2015 through 2019. We also authorize Suburban to issue a Sixth Amendment and Supplement to its existing Indenture of Mortgage and Deed of Trust, in conjunction with the issuance of its new First Mortgage Bonds.

3.3. Encumbrance of Utility Property

Suburban seeks authority to encumber its utility assets in order to secure its new First Mortgage Bonds, pursuant to Pub. Util. Code § 851. In relevant part, Pub. Util. Code § 851 states that no utility shall encumber any part of its plant, system, or other property necessary or useful in the performance of its duties to the public, or any franchise or permit or right there under without first having secured from the Commission an order authorizing it to do so. Consistent with D.04-04-051 and Pub. Util. Code § 851, we authorize Suburban to sell, lease, assign, mortgage, or otherwise dispose of or encumber its utility property, in order to secure its new First Mortgage Bonds.

3.4. Request for Exemption from the New Financing Rule

The New Financing Rule set forth in D.12-06-015, replaced the Competitive Bidding Rule authorized in Resolution F-616 in 1986. The New Financing Rule provides for exemptions based on a compelling showing by the utility that it qualifies for one of the exemptions listed in Attachment A, page A-6 of D.12-06-015. In the current application, Suburban requests that it be exempted from the New Financing Rule because its request for new debt of \$25 million is much less than the baseline dollar amount for applicability of the New Financing Rule of more than \$42 million. We therefore authorize an exemption from the New Financing Rule for Suburban's issuance of its new First Mortgage Bonds.

4. Fee

Whenever the Commission authorizes a utility to issue debt, the Commission is required to charge and collect a fee pursuant to Pub. Util. Code §§ 1904(b) and 1904.1. On December 15, 2015, Suburban remitted the required \$18,500 fee to the Commission's Fiscal Office.⁵

5. Financial Information

We place Suburban on notice that the reasonableness of any resulting interest rate and cost of money arising from debt capital and capital structures are normally subject to review in the appropriate cost of capital or general rate case proceeding. Therefore, we will not make a finding in this decision of the reasonableness of the projected capital ratios for ratemaking purposes. We also will not make a finding in this decision on the reasonableness of Suburban's proposed construction program. Construction expenditures and the resulting

plant balances in rate base are issues that are normally addressed in a general rate case or specific application. The authority to issue securities is distinct from the authority to undertake construction or the right to recover the cost of capital in rates.

6. California Environmental Quality Act

Under the California Environmental Quality Act (CEQA) and Rule 2.4 of the Commission's Rules of Practice and Procedure (Rules), we must consider the environmental consequences of projects that are subject to our discretionary approval.⁶ Thus, we must consider whether approval of this application will alter an approved project, result in new projects or change operations in ways that have an environmental impact.

According to Suburban, it is unknown at this time what the specific project activities and new construction associated with the authority to issue debt will be. The application specifies that the purpose of the application is to secure approval for new First Mortgage Bonds, to be used partly for capital expenditures. Suburban has general plans for the use of the proceeds from the new First Mortgage Bonds, but it does not have the basic details regarding those contemplated projects. Suburban simply possesses inadequate basic information regarding future projects that might be financed through the contemplated new First Mortgage Bonds. However, securing the financing authority now will put Suburban in a better position to undertake plant improvements without delay when construction plans are finalized.

⁵ The fee is assessed on \$25 million of authorized Debt Securities as follows:

$\$2 \times (\$1,000,000/\$1,000) + \$1 \times (\$9,000,000/\$1,000) + \$0.50 \times (\$15,000,000/\$1,000) = \$18,500.$

⁶ Public Resources Code § 21080.

Suburban is aware and states in the application that the utility will comply with all environmental permitting requirements applicable to the construction and improvements that it will undertake in conjunction with the proposed issuance of new First Mortgage Bonds.

Since the details of the proposed improvements are unknown at this time, we will put Suburban on notice that our approval to issue new First Mortgage Bonds does not constitute an implied or expressed waiver of applicable environmental regulations.

This decision does not authorize any capital expenditures or construction projects. New construction projects which Suburban intends to finance via this application should undergo a CEQA review as early as feasible in the planning process, as required by CEQA Guidelines Section 15004(b). Ongoing projects have already been subject to any necessary CEQA review undertaken prior to Suburban receiving a certificate of public convenience and necessity (CPCN) or permit to construct. To the extent capital expenditures are financed with the proceeds of the long-term debt issued pursuant to this decision, CEQA review should occur as needed through the regulatory processes applicable to each capital project.

7. Category and Need for Hearings

By Resolution ALJ 176-3348, dated December 18, 2014, the California Public Utilities Commission (Commission) preliminarily determined that this was a ratesetting proceeding and that a hearing would not be necessary.

Based on the record, we affirm that this is a ratesetting proceeding, and that a hearing is not necessary.

8. Waiver of Comment Period

This is an uncontested matter in which the decision grants the relief requested. Accordingly, pursuant to Pub. Util. Code § 311(g)(2) and Rule 14.6(c)(2) of the Commission's Rules of Practice and Procedure, the otherwise applicable 30-day period for public review and comment is waived.

9. Assignment of Proceeding

Michael Picker is the assigned Commissioner and Seaneen M. Wilson is the assigned ALJ in this proceeding.

Findings of Fact

1. The difference between Suburban's need of \$82.4 million and funds available of \$57.4 million, results in a need for new First Mortgage Bonds of \$25 million.
2. First Mortgage Bonds are a form of long-term debt.
3. Suburban plans to use its new First Mortgage to meet its future financing needs, including: discharge of existing debt; reimbursement of its treasury for capital expenditures; funding of construction, completion, and improvement of facilities; and acquisition of utility property.
4. The Commission does not, by this decision, determine that Suburban's construction budget, cash requirements forecast, and capital structure are necessary or reasonable for ratemaking purposes. These issues are normally reviewed and authorized in general rate case or cost of capital proceedings.
5. In part, the New Financing Rule governs the exemption of utilities from its authority for specific reasons.
6. Suburban's request is in compliance with Pub. Util. Code §§ 816, 817, 818, 824, and 851.

7. Suburban remitted a check for \$18,500 on December 15, 2014, as required by Pub. Util. Code §§ 1904(b) and 1904.1.

Conclusions of Law

1. Suburban should be authorized to issue new Series F First Mortgage Bonds of \$25 million pursuant to the following terms:

- a. Be direct obligations of Suburban;
- b. Rank equally with other of Suburban's First Mortgage Bonds issued under the Indenture;
- c. Have semi-annual interest payments;
- d. Be redeemable prior to maturity, in whole or in part, (a) at the option of Suburban at any time on not more than sixty and not less than thirty days prior notice, at par plus accrued interest, plus the Make-Whole Amount, if any, and (b) upon receipt of proceeds equal to or exceeding \$25,000,000 by the trustee under the Indenture as a result of a casualty or condemnation, at the option of Suburban at par plus accrued interest, without the Make-Whole Amount;
- i. The Make-Whole Amount is the excess amount of the discounted value of the remaining scheduled payments for the principal called for redemption over the amount of such called principal.
- ii. The Make-Whole Amount may in no event be less than zero. For purposes of the discounted value, the rate is equal to the interpolated yield of a U.S. Treasury security with a maturity equal to the remaining life of the called bonds + 50 basis points.

2. Suburban should be authorized to issue a Bond Purchase Agreement associated with the issuance of new Series F First Mortgage Bonds

3. Suburban should be authorized to execute a Sixth Amendment and Supplement to Suburban's existing Indenture of Mortgage and Deed of Trust.

4. The Commission has broad discretion under Pub. Util. Code § 816 et seq., to determine if a utility should be authorized to issue debt securities. Where necessary and appropriate, the Commission may attach conditions to the issuance of debt securities and stock to protect and promote the public interest.

5. In part, pursuant to Pub. Util. Code § 816, the Commission, as vested by the state, may prescribe regulations and restrictions on the issuance of debt and equity securities issues by public utilities, and supervise and control their issuance.

6. The proper term for securities issued pursuant to Pub Util. Code § 817 is greater than 12 months. Pursuant to Pub. Util. Code § 817, a public utility may only issue and use financing for selected purposes. Those purposes not listed in Pub. Util. Code § 817 may only be paid for with funds from normal utility operations.

7. Pursuant to Pub. Util. Code § 824, the Commission may require, in part, that public utilities account for the disposition of the proceeds of all sales of stock and debt. Pursuant to this code section, the Commission may also establish rules to insure the disposition of such proceeds are for the purposes required by the authorizing order.

8. In relevant part, Pub. Util. Code § 851 states that no utility shall encumber any part of its plant, system, or other property necessary or useful in the performance of its duties to the public, or any franchise or permit or right there under without first having secured from the Commission an order authorizing it to do so.

9. CEQA applies to projects that require discretionary approval from a governmental agency, unless exempted by statute or regulation.

10. It is long established that the act of ratemaking by the Commission is exempt from CEQA review.

11. As stated in the California Public Resources Code, Public Resource Code § 21080(b)(8), the “establishment, modification, structuring, restructuring or approval of rates, tolls, fares, or other charges by public agencies” is exempt from CEQA.

12. Suburban should not use the proceeds from the new First Mortgage Bonds authorized by this order to fund its capital projects until it has obtained all required approvals for the projects, including any required environmental review under CEQA.

13. The order herein should not involve any commitment to any specific project which may result in a potentially significant impact on the environment; thus it is not a project subject to CEQA.

14. Application 14-12-011 should be closed.

O R D E R

IT IS ORDERED that:

1. Suburban Water Systems (Suburban) is authorized to issue new Series F First Mortgage Bonds of \$25 million pursuant to the following terms:

- a. Be direct obligations of Suburban;
- b. Rank equally with other of Suburban’s First Mortgage Bonds issued under the Indenture;
- c. Have semi-annual interest payments;

- d. Be redeemable prior to maturity, in whole or in part,
 - (a) at the option of Suburban at any time on not more than sixty and not less than thirty days prior notice, at par plus accrued interest, plus the Make-Whole Amount, if any, and
 - (b) upon receipt of proceeds equal to or exceeding \$25,000,000 by the trustee under the Indenture as a result of a casualty or condemnation, at the option of Suburban at par plus accrued interest, without the Make-Whole Amount;
- i. The Make-Whole Amount is the excess amount of the discounted value of the remaining scheduled payments for the principal called for redemption over the amount of such called principal.
- ii. The Make-Whole Amount may in no event be less than zero. For purposes of the discounted value, the rate is equal to the interpolated yield of a U.S. Treasury security with a maturity equal to the remaining life of the called bonds + 50 basis points.

2. Suburban Water Systems is authorized to issue a Bond Purchase Agreement associated with the issuance of new Series F First Mortgage Bonds.

3. Suburban Water Systems is authorized to issue a Sixth Amendment and Supplement to Suburban's existing Indenture of Mortgage and Deed of Trust.

4. Suburban Water Systems shall not use the proceeds from the new First Mortgage Bonds authorized by this order to fund its capital projects until it has obtained all required approvals for the projects, including any required environmental review under California Environmental Quality Act.

5. Application 14-12-011 is closed.

This order is effective today.

Dated _____, at San Francisco, California.